

COMPETITION AMONG COOPERATIVES

V. James Rhodes*

No issue brings to the fore more incisively one's conception of the basic character of cooperatives and of their role in the market system than the question as to whether each of them engaged in a particular type of operation should have an exclusive territory. (Heflebower, p. 195)

Is competition among cooperatives a good thing? To many readers, the answer will seem so obviously yes that there is no point in pursuing the matter. The merits of competitive markets in providing efficiencies are well-known. Note, however, that the question is not about abandoning competitive markets or creating cooperative monopolies but about the relationships among a special type of firms competing in a market. It is not at all unusual for competing firms to merge, and even when one or both firms are relatively large, the merger is often judged by the Department of Justice to be acceptable. In most regional or national agricultural markets, the merger of all existing cooperatives would not create a monopoly and frequently would not create a firm that ranked in the top four firms in that market.

Historical Background

Cooperation was regarded early as the antithesis of competition. The slogan of early British cooperators was "cooperation, not competition" (Wiles, pp. 253-54). These early practitioners saw cooperatives as a type of public enterprise with multiple social objectives--objectives that could not be fulfilled if all energies were focused on prices and patronage refunds. As transportation improved in the early 20th century, British cooperative stores encountered more and more overlap among their trade areas. The Cooperative Union campaigned to eliminate this intercooperative competition through negotiation of boundaries or of mergers. Generally these early British leaders felt that competitive overlapping led to wasteful duplication, unsound financial practices, and the erosion of the cooperative spirit (Boner, pp. 98-101 and 340-42).

Transportation improvements in the United States in the past century have led--as in Britain--to more overlapping of the trade areas of local agricultural cooperatives. Such cooperative competition sometimes has led to mergers or to the demise of one or more of the participants, but it has sometimes persisted for many years.

The regional cooperatives rather quickly encountered other regionals as they grew in the 1920s and 1930s. Responses to interregional competition have varied. As one example, Consumers Cooperative Association (CCA) (Farmland Industries' predecessor) overran the rather bitter opposition of the Farmers Unions of Nebraska and Kansas to CCA's solicitation of business from their locals in those states (Fite, pp. 112-15). On the other hand, the Virginia Seed Service (the predecessor of Southern States) withdrew from North Carolina upon the organization of FCX in that area and later withdrew from

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Tennessee as a result of an understanding with Tennessee Farmers (Knapp et al., pp. 535-46).

The only cooperatives with exclusive territories--the rural electric cooperatives (**RECs**) and the Farm Credit System--resulted from government sponsorship in their organization plus the utility nature of the **RECs**. Note that the Farm Credit institutions have much investor-owned competition and that the boundaries limit cooperative competition, not proprietary competition.

On request, Joseph Knapp, the first administrator of the Farmer Cooperative Service, presented a paper on this topic at the 1949 annual meeting of the American Institute of Cooperation. Knapp reported the findings of an informal survey of cooperative managers and outside observers on the subject as well as his own judgments. Knapp found that:

1. Excessive competition among cooperatives was judged to be a problem--often expensive and divisive;
2. Competition also had its good points in keeping managers on their toes and eliminating the inefficient;
3. Excessive competition among cooperatives often was due to managers--their vanity or their empire-building ambition;
4. An ideal cooperative system would not have competition among cooperatives, but that probably is not attainable.

Theoretical Considerations

From society's viewpoint, is any restriction of competition among cooperatives a bad thing? That depends on how much competition would survive among the investor-owned firms (**IOFs**) and the cooperatives. Generally, as suggested earlier, active competition would survive because the market structure is not highly concentrated, product differentiation is often rather small, and entry barriers are moderate or lower. The argument could be carried into less competitive markets. To the extent that a few markets may be highly contestable, competition is adequate even when there is high structural concentration or even monopoly (Rhodes). Moreover, arguments could be made that section 2 of the Capper-Volstead Act can be used to regulate adequately even cooperative monopolies. Without judging the merits of that position, this paper does not go that far. It is simply argued that in most markets the elimination of competition among the cooperatives would not affect the public interest. Where there are exceptions, perhaps competition among cooperatives should be preserved for public policy reasons. **The** next section proceeds on the assumption that there will be adequate competition in the market regardless of how little the competition among the cooperatives.

There also is a criterion of cooperative member welfare as well **as** the public interest. **Is** any restriction of competition among cooperatives a good thing

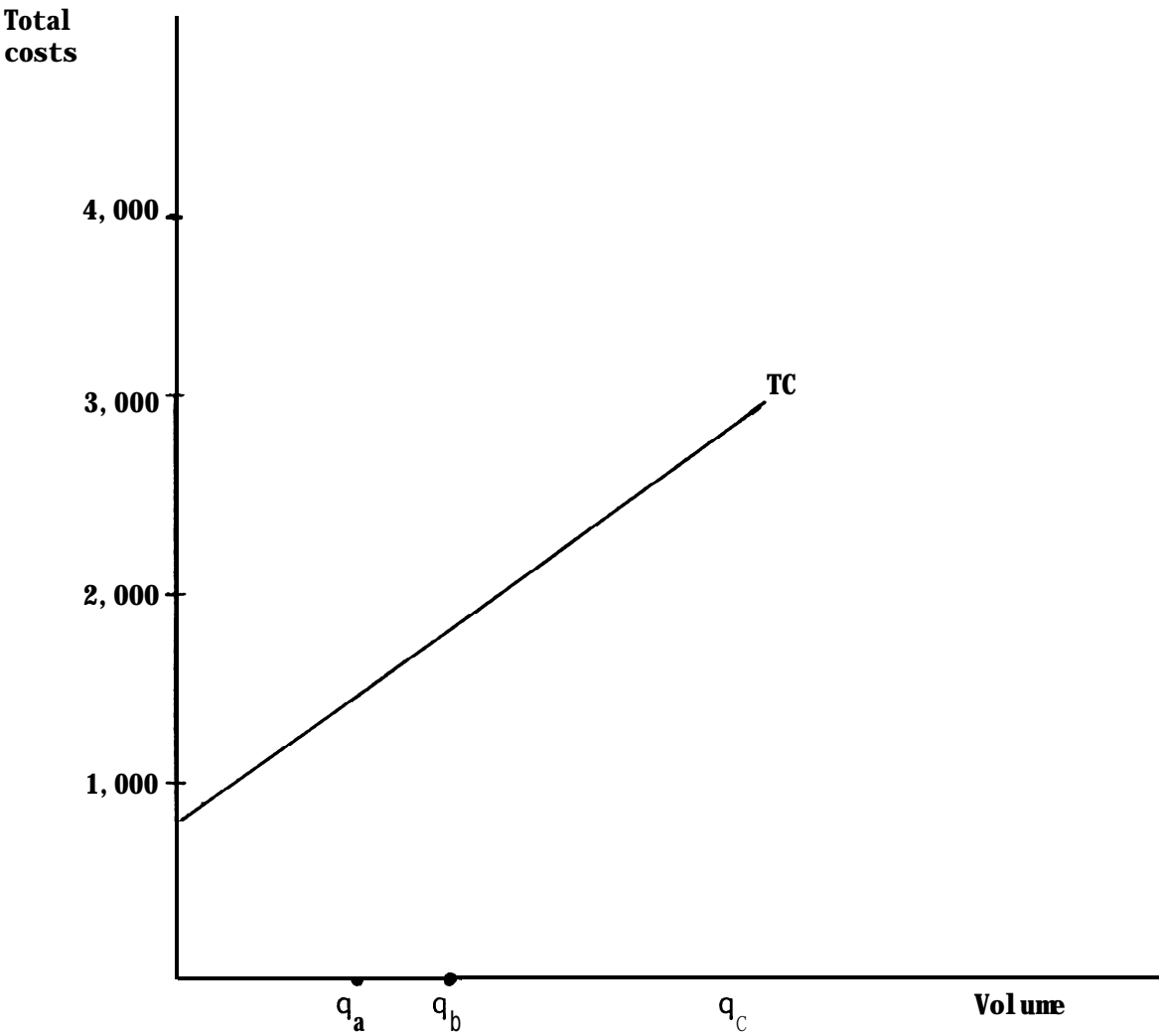
for the members? Would it be economical for a given set of farmers to originate two or more independent cooperatives to compete in hauling their milk, making cheese, marketing grain, or whatever? Generally not. That is, any volume that these farmers demand to be handled has a lower total cost for one firm handling it than would be the combined total cost of two or more firms doing it. In figure 1, output q_c is the output marketed through a single cooperative; output q_b is $1/2 q_c$ and output q_a is $1/3 q_c$; TC is the long-run total cost curve for the most efficient performance of that particular marketing function. It can be seen that $3TC_a > TC_c$ and $2TC_b > TC_c$. It is likely, of course, that there is some output q_d (where $q_d > q_c$) at which the TC is rising faster than a linear rate because of diseconomies of scale and it is no longer efficient for the total volume to be handled by one firm. What is argued here is that this subadditive condition¹ of one firm being the most efficient to serve a given set of farmers is empirically true for many markets.

Likewise it generally would not be economical for a given set of local cooperatives to set up two competing regionals to make their fertilizer, provide them fuel, or market their grain. Because of the costs of duplication of facilities, personnel, and efforts, setting up competing cooperatives ordinarily would not be beneficial for the members. The argument that competition among cooperatives is essential to X-efficiency ("keeping cooperative managers on their toes") is not valid because plenty of competition from the **IOFs** exists with the possible exception of one or two commodities.

Competition among two cooperatives usually involves not one set of farmer-members, but two overlapping sets. The overlap is formed roughly by the members being competed for by both cooperatives. The overlap members may vary from a tiny percent to a majority of all members. Member interests are even less homogeneous. Even boards of each cooperative may have some thoughts of "winning" the competitive battle. Those members being competed for may obtain special prices and services. Those beneficiaries will likely praise cooperative competition. Even if beneficiaries realize their gains are at the expense of the financial health of their organization, they probably can rationalize their gains. For example, those nearing retirement can reason that they merely are getting back some of their investment that they otherwise would not get for a long time.

While farmers as a group clearly may benefit from cooperation among cooperatives, their members may focus more on individual payoffs. The problem is the same in any coalition. There is a natural struggle over the division of the benefits. An individual is likely to focus on his or her return rather than on the group's total returns. An individual is not likely to consider whether action to increase their own return may reduce the total group return. He or she may be caught in a fallacy of composition in which they presume that individual gains translate into group gains rather than the opposite. If an individual does consider and does perceive the negative relationship of individual and group returns, he or she does not necessarily restrain himself or herself. The individual may justify his or her action by arguing that others will take similar advantage of the situation. The possibility of beggaring thy fellow member is the reason that citizens may

Figure 1



voluntarily vote a compulsory tax, or farmers may voluntarily vote the compulsions of a marketing order. While various cooperative rules and state and federal legislation ameliorate the individual-group conflicts within a cooperative, various members persist in using competitive market place opportunities (IOF as well as cooperative) as a way to enhance their individual bargaining power and economic returns. If there were an institution similar to a marketing order to minimize cooperative competition, members could avoid the prisoner's dilemma they now face.²

What will be the outcome of this conflict of interests? Will the cooperative spirit (the community of interest) of all farmers cause members to object to the cooperative competition? Will their objections affect cooperative policy? Answers must be empirical. On the European continent, agricultural cooperative competition generally is not permitted (Straub). Some of that restriction may arise from the intervention of government or other supracooperative organizations as well as from the solidarity among farmer-members (Foxall). That is, the Europeans generally have developed the institutions necessary to solve the problem. In this country, our brief historical survey suggests that "cooperative statesmanship" sometimes prevails. However, competition among cooperatives sometimes is especially aggressive and even vindictive.

Cooperatives and Government Policy

Government policy could range from active intervention to nationalizing a cooperative system (as in some European countries) to stern antitrust attacks on any attempts to reduce competition among cooperatives. The present political climate certainly does not support nationalization. Likely, the government will not be much involved as long as there is general adherence to the antitrust regulations.

What can cooperatives do about reductions in competition if and when desired by membership? A chief remedy for excessive competition would appear to be structural. Mergers and acquisitions can remove many of the worst overlaps of territories and the clash of opposing interests. Managers and boards have their own personal reasons for dragging their feet on mergers and acquisitions, but they feel more comfortable considering structural rather than conduct remedies to excessive competition. Structural consolidation of cooperatives offers much promise in certain areas such as milk assembly and grain marketing, but it has its limitations. Members are concerned about the impacts of structural consolidation on their market outlets, their sources of inputs, their claims to capital in the cooperative, and their influence in governance. These quite legitimate concerns of members tend to hinder structural consolidation even where economies of scale appear favorable. The feasibility of joint ventures or common sales agencies needs to be examined as a halfway step in many situations.

Certain principles of conduct by cooperative board and managers should be considered:

1. Do not build or acquire a facility or enter a market when that effort can only succeed at a substantial cost to another cooperative;
2. Do not dump excess inventories in another cooperative's market;
3. Do not start price wars;
4. Develop the kind of healthy interaction with members and a program of equity rotation so that most members will not consider the cooperative of more value dead than alive;
5. Develop member understanding of the larger payoff available to the group if it is not undermined by excessive competition among cooperatives- -a competition that is often incited or abetted by individual members.

Summary

The "problem" of competition among cooperatives often is discussed by cooperators, but not for publication. Early British cooperators sought a cooperative or socialist system rather than market capitalism. American agricultural cooperators accept the market system and the values of the competitive market.

The question is twofold: (1) Can competition among cooperatives be moderated without damaging the competitive market? (2) If so, does moderation of competition among cooperatives benefit their members? A qualified yes is given to both questions. Most regional and national markets are dominated by IOFs, not cooperatives, and preservation of the competition among the IOFs and between them and the cooperatives is not at question. Ordinarily, a reduction of competition among cooperatives would benefit members as a group. However, such reduction may likely reduce the individual returns of some members who have benefited directly from the competition.

The earlier literature, as shown in Knapp, emphasized that the attention of cooperative managers to their individual goals was a cause of cooperative competition. While that problem remains, more recent thinking emphasizes that membership attention to their individual payoffs may be equally at fault. This prisoner's dilemma can be solved by group solidarity, by farsighted board and management action, or by more far-reaching institutions. The European cooperative solution typically is that of our Farm Credit districts--erect boundaries between cooperatives by regulation. Some regional cooperatives have respected boundaries, but many have not. Ordinarily there are no boundaries to guide local cooperatives. It is not feasible to tell farmers where to market their grain or purchase their supplies. Boards of directors are likely in the best position to appreciate and to push for the maximum long-term payoffs to all cooperative members. It is doubtful that most boards are well enough informed and strong enough to do much about the problem. Thus the problem of competition among cooperatives remains a challenge to educators, cooperative leaders, and those who could design new institutions.

Notes

1. See discussion of subadditivity in chap. 2 of Baumol, Pangar, and Willig.
2. Staatz presents an excellent development of this problem.

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